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W. E. Williams v. H. R. Espey and J. H> Morgan, Sr. : Brief of Appellant

Utah Supreme Court

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In the Supreme Court of the State of Utah

W. E. WILLIAMS,
Plaintiff and Appellant,

vs.

H. R. ESPEY,
Defendant,
and
J. H. MORGAN, SR.
Defendant and Cross Appellant.

Case No. 9251

BRIEF OF APPELLANT

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PRELIMINARY STATEMENT

Reference in appellant's brief to the transcript will be designated by the letter "R." The parties will be referred to as in the court below.

STATEMENT OF FACTS

This case arises out of a transaction entered into in August of 1954 at a time when the uranium "fever" in the State of Utah was reaching epidemic proportions.

Defendant, Espey, a non-resident, contacted plaintiff on August 24, 1954 and asked to borrow up to $10,000.00 from plaintiff (R-43). After some negotiating which will be referred to in more detail later, plaintiff did loan defendant Espey $2,500.00 and in consideration therefore received a promissory note signed by defendant Espey and endorsed in blank by defendant Morgan (Ex. P-2) together with an agreement between defendants Espey and Morgan jointly as first parties and plaintiff as second party (Ex. P. 1). The principal controversy involves the construction of this agreement and the circumstances surrounding it.

In consideration of the loan, the defendants agreed to deliver a note in the sum of $2,500.00 bearing 6% interest for a period of five months and in addition the defendants, pursuant to the agreement, gave plaintiff several options to purchase uranium stocks and/or to receive an interest in certain uranium claims.

Paragraph 1 of the agreement provides:

> "Espey agrees to execute and deliver a Note in the sum of Twenty-Five Hundred Dollars ($2,500.00) bearing six per cent (6%) interest for a period of five (5) months from date hereof. To secure said note, Espey authorizes J. H. Morgan, Sr. to hold for him in trust, seventy-five hundred shares (7500) of the White Canyon Mining Company stock to be delivered to Second Party upon failure to pay the Note when due."

Paragraph 2 of the agreement gave three independent options to plaintiff as additional consideration with the provision that he could elect to choose one of the three.

There is no particular controversy over these three options contained in paragraph 2 inasmuch as plaintiff did not attempt to exercise any of them. However, paragraph 2 contains the following language in addition to the three options referred to:

> "An [as] additional consideration for said loan and irrespective of which option Second Party exercises, First Parties agree to give Second Party an option on twenty-five hundred shares (2500) of White Canyon Mining Company stock at eighty cents (80c) per share, said option to be exercised on or before eighteen (18) months from completion of the public offering."

The note executed by Espey and endorsed by Morgan became due on January 24, 1955, five months after its execution. Plaintiff attempted unsuccessfully to contact defendant Morgan a few days prior to the due date of the note, (R. 46-7) and finally contacted him some time between four to ten days after the due date and made an appointment to meet him in his office. (R. 47) Defendant Morgan was surprised that Espey had failed to pay the note when due and offered to make payment to plaintiff himself. However, when plaintiff pointed out the options contained in the agreement and attempted to exercise the option to purchase the additional 2500 shares of White Canyon Mining Company stock at 80 cents per share, defendant Morgan refused to make any payment and indicated to plaintiff that the agreement in his opinion was usurious and plaintiff left Morgan's office without any satisfaction either by way of cash or stock. (R. 47-49)

Plaintiff then contacted an attorney and as a result

thereof a letter was written to defendants demanding delivery of 7500 shares of White Canyon stock by reason of the failure to pay the note at maturity and also again exercising the option to purchase an additional 2500 shares of White Canyon Mining Company stock at 80 cents per share. (Ex. P-5)

Some time after the action was commenced, Morgan paid $2,500.00 plus interest to the Clerk of the Court. The case was tried to the Court sitting without a jury and the Court found that the 7500 shares of stock held by Morgan was held as security only and that the plaintiff was not entitled to it unless it became necessary to sell the stock to pay the $2,500.00 note. Judgment for $2,500.00 plus interest from August 24, 1955 was entered in favor of plaintiff. The court further found that plaintiff properly exercised his option to purchase an additional 2500 shares of White Canyon Mining Company stock at 80 cents a share, that Morgan refused to deliver the stock to plaintiff, that such refusal damaged plaintiff in the amount of $2,525.00, that sum being the difference between the 80 cent option purchase price and $1.81 which was the price at which plaintiff could subsequently have sold the stock had it been delivered to him. The court also awarded $500.00 attorney's fees.

Plaintiff appealed from the court's Finding and Conclusion that the 7500 shares of stock was to be held as security only, it being plaintiff's contention that the stock should have been delivered by Morgan to plaintiff since the note was not paid when due and that plaintiff is entitled to all right, title and interest in and to said stock and that the

failure to so deliver the stock upon default in payment of the note, constituted a conversion thereof by Morgan.

Defendant Morgan has cross-appealed contending that the court erred in awarding damages in the amount of $2,525.00 for the wrongful refusal of defendants to allow plaintiff to exercise his option to purchase 2500 shares of White Canyon Mining Company stock at 80 cents per share and also contending that plaintiff is not entitled to the attorney fees awarded.

STATEMENT OF POINTS

POINT I.

THE TRIAL COURT ERRED IN FINDING THAT THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK WAS HELD BY DEFENDANT MORGAN AS SECURITY ONLY.

POINT II.

THE TRIAL COURT ERRED IN FAILING TO FIND THAT PLAINTIFF WAS ENTITLED TO ALL RIGHT, TITLE AND INTEREST TO THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK UPON FAILURE OF DEFENDANTS TO PAY THE NOTE ON MATURITY.

POINT III.

THE TRIAL COURT ERRED IN FAILING TO FIND THAT THE REFUSAL TO DELIVER THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK TO PLAINTIFF UPON FAILURE TO PAY THE NOTE CONSTITUTED A CONVERSION THEREOF BY DEFENDANT MORGAN.

POINT IV.

THE TRIAL COURT ERRED IN FAILING TO AWARD TO PLAINTIFF THE ADDDITIONAL SUM OF $13,575.00 FOR DAMAGES RESULTING FROM DEFENDANT MORGAN'S WRONGFUL REFUSAL TO DELIVER 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK TO PLAINTIFF UPON DEFAULT OF PAYMENT OF THE PROMISSORY NOTE.

ARGUMENT

POINT I.

THE TRIAL COURT ERRED IN FINDING THAT THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK WAS HELD BY DEFENDANT MORGAN AS SECURITY ONLY.

In determining the effect of the agreement under consideration, we think it important to keep in mind the circumstances surrounding the transaction. Defendant Espey was a uranium promoter. He was a non-resident of this state and a complete stranger to plaintiff. He voluntarily contacted plaintiff on August 24, 1954 (R. 40) for the purpose of raising money to finance various uranium ventures (R. 42, 43) and originally asked plaintiff for $10,000.00. Plaintiff explained that he was not in the business of loaning money, that he was not interested in loaning money, that it would be foolish to loan that kind of money for such a purpose to a complete stranger, whereupon defendant Espey volunteered to include as consideration for the money various stock options and as a result plaintiff indicated that if some local citizen with a good reputation would stand behind the transaction, he might possibly go along. Mr. Espey volunteered Mr. Morgan's

name and indicated he would talk to him and call back on plaintiff the same day. (R. 43-44)

Espey returned with the note and agreement which are the subject of this action and which are identified as plaintiff's Exhibits 1 and 2.

Paragraph 1 of the agreement provides that in consideration of the loaning of the money,

> "Espey agrees to execute and deliver a note in the sum of Twenty-five Hundred Dollars ($2500.00) bearing six per cent (6%) interest, for a period of five (5) months from date hereof. To secure said Note Espey authorizes J. H. Morgan, Sr. to hold for him in trust seventy-five hundred shares (7500) of the White Canyon Mining Company stock to be delivered to Second Party upon failure to pay the Note when due."

It is this language which the court construed in holding that the 7500 shares of stock was held as security only. Plaintiff earnestly contends that such finding was in error and that the court should have found that the stock was not held as security but was held in trust by Morgan to be delivered to plaintiff in the event the note was not paid at maturity and that plaintiff was entitled to all right, title and interest thereto.

While it is true the language of the instrument uses the words "to secure" we think those words are unimportant when the agreement is properly construed and we think it clearly was not the intent of the parties that the 7500 shares of stock represent a pledge of security only.

It is important to bear in mind that defendants Morgan and Espey are co-obligors in this agreement and that the stock was delivered from Espey to Morgan to hold in *trust* to be delivered to plaintiff *if and only if* the note was not paid at maturity. In other words, the possession of the stock was never in plaintiff (and plaintiff has not yet received one share thereof) and under the terms of the agreement, plaintiff was not even entitled to possession until and unless the note was not paid at maturity.

The whole theory behind a pledge of security is that possession is transferred immediately to the obligee, so that if the obligor does not perform, the obligee then merely has to liquidate the security and retain from the liquidated funds the amount of the debt. However, where possssion is not transferred from the obligor or debtor to the creditor or obligee, it is obvious there is no pledge of security involved. There appears to be no conflict in the law on this subject.

In 41 Am. Jur., 586, it is stated:

> "the essential elements and requisites of a pledge are (1) the existence of a debt or obligation, and (2) *the transfer of property to be held as security,* and, if necessary, used, for the payment thereof." (Emphasis added)

This court in the case of *Campbell v. Peter,* 108 Utah 565, 162 Pac. 2d 754 held:

> "A pledge . . . is the passing of the possession of a chattel by the owner thereof to the pledgee who is thereby entitled to hold it until the debt is paid

or the obligation performed."

The mere characterization of a transaction as "security," "collateral" or "pledge" does not make it such, the intention of the parties as to the nature of the transaction is the controlling element. In 41 Am. Jur., 585 it is stated:

> "This intention or conduct is ascertained from the whole instrument evidencing the transaction, and not from particular words therein. Thus, the fact that the word 'pledge' is employed in an instrument evidencing a transaction does not conclusively determine its character. . ."

It has consistently been held delivery is essential to a valid pledge. The court in *Hodge v. Truax,* 184 Wash. 360, 51 Pac. 2d 357 stated;

> "One of the prime requisites of a pledge is that the pledgor has parted with his property and that the pledgee has possession or control over it."

This court in *Campbell v. Peter,* supra, stated:

> "A pledge to be valid depends upon possession by the pledgee or his agent, either actual or constructive, of the chattel at all times until the fulfillment of the obligation which it secures. . . Possession is an essentional element of a pledge and without it there can be no pledge."

These principles are forcefully set forth in 41 Am. Jur., 592-593 as follows:

> ". . . it is essential to a consummated contract of pledge that there shall have been a delivery of the pledged property, either actual or constructive, to the pledgee or to a pledge holder. Good faith does

> not avail the pledgee either actual or constructive. Until the act of delivery has been performed the special property which the pledgee is entitled to hold does not vest in him. The requirement of possession is an inexorable rule of law, . . . Generally, delivery must have been as complete as the nature of the property permits. The pledgee's possssion, to be effective either for notice or to give validity at law to the pledge, must be complete, unequivocal, and exclusive of the pledgor's possession in his own right."

Actual delivery to and possession by the creditor is a prime requisite in order to constitute a pledge. It is possible, however, that delivery can be made to a third person for and on behalf of the creditor to constitute a constructive delivery, but it is apparent that such was not the case here. Morgan, the so-called pledge holder, was not selected by plaintiff as is required by law in order to constitute a constructive delivery. See 41 Am. Jur., 599. In fact, Morgan was a co-obligor in the agreement and a close associate of defendant Espey. Further, the language of the agreement itself gives plaintiff no right to the requisite possession unless and until the note is not paid at maturity, nor was Morgan authorized to deliver the stock to plaintiff until that time. Certainly this is not constructive delivery in any sense.

Where there is a close relationship beween the pledgor and the stake holder, the alleged fulfillment of the requirement of delivery should be carefully scrutinized in view of the real danger that the actual control may never be surrendered by the debtor-pledgor. In the instant case there was and is such a close relationship

between defendants Espey and Morgan. They are co-obligors in this transaction, both having signed the promissory note and they together constitute "parties of the first part" for the purposes of the agreement under consideration. They are also closely associated as stockholders of the White Canyon Mining Company. The closeness of the relationship indicates that the pledgor herein never relinquished actual control over the stock.

The Supreme Court of Washington passed on this type situation in the case of *Kietz v. Gold Point Mines, Inc.* 105 Pac. 2d, 71. In that case the plaintiff loaned a thousand dollars to defendant company and entered into agreement whereby it was clearly spelled out that 25,000 shares of stock was to be pledged and assigned to plaintiff as security for the note and the agreement further spelled out the intent of the parties by indicating that plaintiff was to transfer the stock back to defendant upon payment of the note. The stock certificate, however was retained by the secretary of the defendant corporation. The court held that there was no pledge of the stock because possession had not been transferred to plaintiff. The following language is, we think, important:

> "In passing upon the question of necessity of delivery of personal property to complete a pledge, this court stated in *Kuhn v. Groll,* 118 Wash. 285, 203 P. 44, 47:
>
> 'It is true that the law requires a delivery of the pledged property from the pledgor to the pledgee and a retention of it by the pledgee in order to make the pledge fully effectual as security. We think the law applicable to the situation we find here is well stated in 21 R.C.L. 643, as follows:

> ' "The requirement of possession is an inexorable rule of law, adopted to prevent fraud and deception, for, if the debtor remains in possession, the law presumes that those who deal with him do so on the faith of his being the unqualified owner of the goods." ' "

It is essential to the existance of a constructive pledge that the pledgee creditor have the *continuous* right to possession of the pledged article. This, of course, was not the case herein. The very fact that it is necessary to sue for possession of the stock in question, indicates that the creditor herein has not had and does not have the actual or constructive possession of the stock in question.

This litigation is not the usual type which arises in the case of a pledge. In the typical case it is the pledgor who must sue the pledgee for return of the article which was transferred for security, but here since possession was never transferred, it is the creditor who now is forced to sue for possession of the stock to which he was clearly entitled upon default in payment of the note.

The language of this agreement is in the alternative. The obligors, defendants Morgan and Espey intended to be able to discharge the $2,500.00 obligation by delivery of the stock, should it be reduced in value. In other words, the agreement gives defendants the choice of paying the note when due or in lieu thereof delivering the stock.

A finding that the stock was not given as security but was in fact to be given in lieu of payment of the note, at the option of the defendants, is not only compelled by

the law, but also by the facts surrounding the transaction. Mr. Williams testified that he was not in the business of loaning money and certainly would not loan money to a stranger at 6% interest. (R. 43) He further testified that it was his understanding that if the stock had gone down in value, the defendants could have satisfied their obligation to him insofar as the $2,500.00 loan was concerned by delivering 7500 shares of stock. If in fact the stock had been worth less than $2,500.00 at the time the note was due, there is no doubt but that the defendants would have satisfied their obligation by transferring the 7500 shares of stock to plaintiff. Plaintiff was willing to take the gamble of such a transaction with the hope that even should he be forced to accept the stock with a then value less than the note amount, the stock would subsequently achieve a substantial increase in value. Furthermore, it is important to remember that the defendants gave plaintiff several other options covering other stocks as additional consideration for advancing the $2,500.00 and the transaction took place during the highly speculative period involving the uranium boom in Utah. At that time uranium stock values were an unknown factor and fluctuated wildly.

The total lack of delivery of the alleged "security" to either the creditor or to a bona fide pledge-holder coupled with the clear import of the language of the agreement that the 7500 shares of stock were to be paid over in their entirety upon default of payment of the note, cannot but compel the conclusion that the stock was not given Morgan as security.

POINT II.

THE TRIAL COURT ERRED IN FAILING TO FIND THAT PLAINTIFF WAS ENTITLED TO ALL RIGHT, TITLE AND INTEREST TO THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK UPON FAILURE OF DEFENDANTS TO PAY THE NOTE ON MATURITY.

Insofar as the 7500 shares of stock is concerned, defendant Morgan is a mere naked trustee and nothing more. The alternative agreement authorizes Morgan to hold the stock in trust for Espey to be delivered to plaintiff upon failure to pay the note when due. (Defendant Espey did not appear at the trial and has been heard from only once, by telephone, since the transaction was entered into, and then some one and one-half to two years after the transaction. (R. 45) Counsel for both defendants indicated the whereabouts of Espey was and is unknown and that he may well be dead (R. 36 & 61). This agreement gave Morgan no right or interest whatever in the stock. It remained the property of Espey until and unless given over to plaintiff. Morgan's obligation with respect to the stock is clearly set forth in the agreement. In the event the note was paid, he was, as trustee, to return it to defendant Espey. In the event the note was not paid at maturity, he was to deliver it absolutely and with no qualifications to plaintiff. Under no circumstances could he claim it as his own.

There can be no question that the note was not paid at maturity and that actions of Morgan when demand was made for payment do *not* constitute an offer of payment.

When Mr. Williams called on defendant Morgan in connection with this transaction approximately one week to 10 days after the note was due, it is true that Morgan initially made an offer to make payment of the $2,500.00. But this offer was clearly conditional inasmuch as when plaintiff mentioned the options connected with the agreement, defendant Morgan, although expressing no concern in connection with the Coyote interest, totally refused *all* payment when plaintiff mentioned the White Canyon option on page 2 of the agreement granting plaintiff the option to purchase an additional 2500 shares of White Canyon stock at 80 cents per share. Upon mention of this option, Morgan immediately withdrew his offer to make payment of the note and said: "I'll see you in hell first on that one. You will not get it." (R. 48)

It is elementary that a conditional tender is ineffectual.

Williston on Contracts, Revised Edition, Volume 6, Section 1814 states:

> ". . . a tender of performance of an absolute obligation of the debtor must be unconditional, since the debt itself is unconditional. No tender can be effective if its acceptance would prejudice the creditor's rights;"
>
> "Therefore, a condition that a payment shall be taken in full discharge or as a compromise of the debtor's obligation, or that the creditor shall give a receipt in full of all demands, . . . invalidates a tender."

This court has held that a tender of less than the amount due, if refused, has no legal significance and that nothing short of everything that the creditor is entitled to receive is a sufficient tender. *Siverts v. White,* 2 Utah 2d 351, 273 Pac. 2d, 974. See also the annotation in 5 A. L. R. 1226 which cites the general rule that:

> "A tender must include everything to which the creditor is entitled, and a tender of any less sum is nugatory and ineffective as a tender."

See also 52 Am. Jur., 230.

The offer by Morgan to make payment of the note alone was conditioned upon plaintiff's willingness to waive this right and relinquish this option. Certainly such a tender is totally ineffective.

The court properly found that plaintiff did exercise this option to which he was unquestionably entitled regardless of whether Morgan paid the note or gave up the 7500 shares of stock, and that the failure of defendant Morgan to sell the stock to plaintiff at the option price resulted in plaintiff's damage in the amount of $2,525.00. Since plaintiff has been held by the lower court to be fully entitled to exercise the option, it is apparent that the tender of payment of the note conditioned upon the waiver of that right was no tender at all. We submit, therefore, that the note payment was in default and that upon such default by the clear intent of the contract, plaintiff was entitled to have the stock delivered to him according to the terms of the agreement and that such delivery should pass all right, title and interest thereto in lieu of the payment of the promissory note.

POINT III.

THE TRIAL COURT ERRED IN FAILING TO FIND THAT THE REFUSAL TO DELIVER THE 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK TO PLAINTIFF UPON FAILURE TO PAY THE NOTE CONSTITUTED A CONVERSION THEREOF BY DEFENDANT MORGAN.

The 7500 shares of stock in question do not under any circumstances belong to defendant Morgan. He is merely a trustee or at least a bailee with instructions to hold the stock for the use and benefit of Espey until the note matures and at maturity, in the event the note is not paid, to deliver the stock to plaintiff. The wrongful refusal to deliver the stock to plaintiff upon failure to pay the note at maturity, constitutes a conversion thereof. The general rule is stated in 53 Am. Jur., 822 as follows:

> "The gist of a conversion has been declared to be not the acquisition of the property by the wrongdoer, but the wrongful deprivation of a person of property to the possession of which he is entitled. A conversion consists of an act in derogation of the plaintiff's possessory rights, and any wrongful exercise or assumption of authority over another's goods, depriving him of the possession, permanently or for an indefinite time, is a conversion."

This court in the case of *Christensen v. Pugh,* 84 Utah 440, 36 Pac. 2d 100, quoted with approval the definition found in 2 Greenleaf on Evid. Section 642 as follows:

> "Conversion consists either in the appropriation of a thing to the party's own use and beneficial enjoyment, or in its destruction, or in exercising do-

> minion over it, in exclusion or defiance of the owner's right, or in withholding the possession of the property from the owner under a claim of title inconsistent with his own."

The court went on to say:

> "The gist of conversion is not the acquisition of property by a wrongdoer, but the wrongful deprivation of it to the owner."

We submit that there can be no question concerning Morgan's conversion of the stock.

POINT IV.

THE TRIAL COURT ERRED IN FAILING TO AWARD TO PLAINTIFF THE ADDDITIONAL SUM OF $13,575.00 FOR DAMAGES RESULTING FROM DEFENDANT MORGAN'S WRONGFUL REFUSAL TO DELIVER 7500 SHARES OF WHITE CANYON MINING COMPANY STOCK TO PLAINTIFF UPON DEFAULT OF PAYMENT OF THE PROMISSORY NOTE.

Plaintiff introduced, without objection by defendants, a letter from J. A. Hogle and Company, (Ex. P-4) indicating that the highest market value of the White Canyon Mining Company stock was reached on October 16, 1955, some nine months after plaintiff was entitled to the stock—that price being $1.81 per share.

The measure of damages for conversion of a chattel of fluctuating value is the highest market value between the conversion and either a reasonable time thereafter or between the conversion and the date of trial. See 53 Am.

Jr., 891; 40 A. L. R. 1288 and 87 A. L. R. 818. The high market value of $1.81 occurring only nine months from date of conversion would allow plaintiff to recover at that figure under either rule stated above.

On the basis of the evidence and the above rule, the trial court properly assessed plaintiff's damages for defendants' failure to allow exercise of the option to purchase 2500 shares on the basis of $1.01 per share, the difference between the option price of $.80 and the high market value of $1.81. Utilizing this same evidence and rule of law plaintiff's damage for the withholding of the 7500 shares of stock amounts $13,575.00. Plaintiff should have received 7500 shares of stock, upon the failure to pay the note, at no cost hence his damage by defendant Morgan's wrongful refusal amounts to a loss of the full price of $1.81 for each of the 7500 shares wrongfull withheld, or $13,575.00.

Defendant failed to raise any objection to this measure of damage either at the trial or in connection with the points raised on appeal.

CONCLUSION

Plaintiff contends that the trial court committed reversible error in holding that the 7500 shares of White Canyon Mining Company stock was held by defendant Morgan as security only and that under the contract and the circumstances surrounding the execution thereof, it is clear that the stock was not pledged as security but was given to defendant Morgan in trust to be delivered to plaintiff with full right, title and interest thereto in the

event the note was not paid. The note was not paid and has not been paid and defendant Morgan has wrongfully converted the stock to his own use and deprived plaintiff of it thereby preventing plaintiff from selling same at the high market value of $1.81 per share, damaging plaintiff in the sum of $13,575.00 rather than the $2,500.00 plus interest as payment of the note, awarded by the court.

Plaintiff respectfully submits that the trial court's decision insofar as it considered the 7500 shares of stock as security should be reversed and judgment entered in favor of plaintiff for $13,575.00 damages for the wrongful conversion of said stock in addition to the attorney's fees awarded and the $2,525.00 awarded for the option stock.

Respectfully submitted,

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